

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
635 Associates : AFFIDAVIT OF MAILING

for Redetermination of a Deficiency or a Revision :
of a Determination or a Refund of Unincorporated :
Business Tax under Article 23 of the Tax Law for :
the Years 1971 - 1975. :

State of New York
County of Albany

Jay Vredenburg, being duly sworn, deposes and says that he is an employee of the Department of Taxation and Finance, over 18 years of age, and that on the 29th day of January, 1982, he served the within notice of Decision by certified mail upon 635 Associates, the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

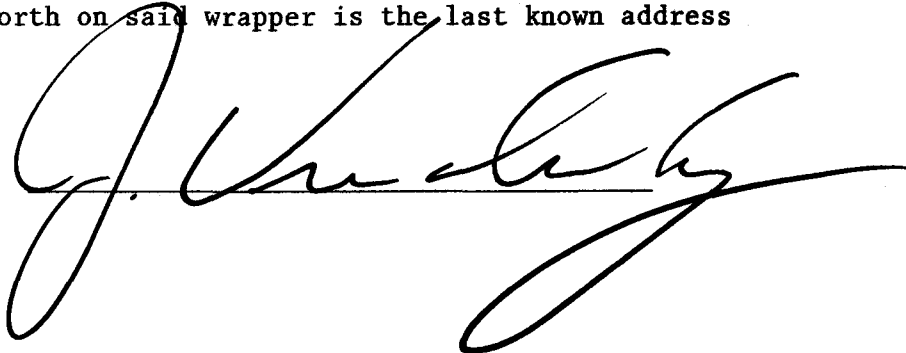
635 Associates
c/o Philip Smith
440 Park Ave. South
New York, NY 10016

and by depositing same enclosed in a postpaid properly addressed wrapper in a (post office or official depository) under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the petitioner herein and that the address set forth on said wrapper is the last known address of the petitioner.

Sworn to before me this
29th day of January, 1982.





STATE OF NEW YORK
STATE TAX COMMISSION

In the Matter of the Petition
of

635 Associates

:

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AFFIDAVIT OF MAILING

for Redetermination of a Deficiency or a Revision :
of a Determination or a Refund of Unincorporated
Business Tax under Article 23 of the Tax Law for :
the Years 1971 - 1975.

State of New York
County of Albany

Jay Vredenburg, being duly sworn, deposes and says that he is an employee of the Department of Taxation and Finance, over 18 years of age, and that on the 29th day of January, 1982, he served the within notice of Decision by certified mail upon Paul J. Koningsberg the representative of the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Paul J. Koningsberg
Koningsberg, Wolf & Co.
200 Madison Ave.
New York, NY 10016

and by depositing same enclosed in a postpaid properly addressed wrapper in a (post office or official depository) under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the representative of the petitioner herein and that the address set forth on said wrapper is the last known address of the representative of the petitioner.

Sworn to before me this
29th day of January, 1982.

James A. [Signature]

J. Vredenburg

STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

January 29, 1982

635 Associates
c/o Philip Smith
440 Park Ave. South
New York, NY 10016

Gentlemen:

Please take notice of the *Decision of the State Tax Commission* enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 722 of the Tax Law, any proceeding in court to review an adverse decision by the State Tax Commission can only be instituted under Article 78 of the Civil Practice Laws and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance
Deputy Commissioner and Counsel
Albany, New York 12227
Phone # (518) 457-6240

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative
Paul J. Koningsberg
Koningsberg, Wolf & Co.
200 Madison Ave.
New York, NY 10016
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition
of
635 ASSOCIATES
for Redetermination of a Deficiency or
for Refund of Unincorporated Business Tax
under Article 23 of the Tax Law for the
Years 1971 through 1975.

DECISION

Petitioner, 635 Associates, c/o Philip Smith, 440 Park Avenue South, New York, New York 10016, filed a petition for redetermination of a deficiency or for refund of unincorporated business tax under Article 23 of the Tax Law for the years 1971 through 1975 (File Nos. 27328 and 30535).

A formal hearing was held before Robert A. Couze, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on September 29, 1980 at 1:20 P.M. Petitioner appeared by Konigsberg, Wolf & Co., P.C. (Paul Konigsberg, CPA). The Audit Division appeared by Ralph J. Vecchio, Esq. (Angelo Scopellito, Esq., of counsel).

ISSUE

Whether petitioner's acceptance of rental income and/or management fees rendered it subject to unincorporated business tax.

FINDINGS OF FACT

1. The hearing herein was originally scheduled for redetermination of a deficiency or for refund of unincorporated business tax under Article 23 of the Tax Law for the year 1975 only, (File No. 27328); however, because the issue was the same, the parties herein stipulated to include the years 1971, 1972, 1973 and 1974 (File No. 30535). (See: pages 3, 4 & 5, transcript of hearing testimony).

2. Petitioner timely filed New York State partnership returns for the years in issue wherein it indicated the kind of business as being "Real Estate" and wherein it indicated that it was not subject to unincorporated business tax.

3. On March 16, 1979 and on March 13, 1980, the Audit Division issued notices of deficiency against petitioner. The March 16, 1979 Notice of Deficiency was for the tax year 1975 and asserted a deficiency in the amount of \$4,892.80, plus interest. The March 13, 1980 Notice of Deficiency was for the tax years 1971, 1972, 1973 and 1974 and asserted a deficiency, collectively, in the amount of \$34,536.88 plus interest. Annexed to the March 16, 1979 Notice of Deficiency was a Statement of Audit Changes dated January 10, 1978 which stated, in part, as follows:

| | |
|--|--------------|
| "Business income reported | \$117,450.00 |
| Allowance for partners services | 23,490.00 |
| Exemption | 5,000.00 |
| Balance subject to unincorporated business tax | \$ 88,960.00 |

NEW YORK STATE UNINCORPORATED BUSINESS TAX DUE \$4,892.80"

Annexed to the March 13, 1980 Notice of Deficiency was a Statement of Audit Changes dated January 10, 1979 which stated, in part, as follows:

| | <u>1971</u> | <u>1972</u> | <u>1973</u> | <u>1974</u> |
|---------------------------------|-----------------|-----------------|-----------------|-----------------|
| "Total business income | \$99,358.14 | \$81,831.00 | \$67,000.00 | \$539,392.00 |
| Allowance for partners services | 19,871.63 | 16,366.20 | 13,400.00 | 90,000.00 |
| Exemption | <u>5,000.00</u> | <u>5,000.00</u> | <u>5,000.00</u> | <u>5,000.00</u> |
| Balance subject to N.Y.S. UBT | \$74,486.51 | \$60,464.80 | \$48,600.00 | \$444,392.00 |
| UBT at 5½% | \$ 4,096.76 | \$ 3,325.56 | \$ 2,673.00 | \$ 24,441.56 |
| TOTAL UBT DUE | | | | \$34,536.88" |

4. The petition for a redetermination of the March 16, 1979 Notice of Deficiency and the petition for a redetermination of the March 13, 1980 Notice of Deficiency were both timely filed.

5. In 1968, the land at 635 Madison Avenue in New York City was owned by one Samuel Weinberg as Trustee. The lease on the land and the building thereon was held by Jacobs & Kaufman who sublet same to an organization known as the Milstein Organization. The lease on said property was to expire in the year 2053. The building consisted of nineteen (19) stories with a basement and sub-basement and contained many commercial tenants.

6. In April 1968, the Milstein Organization sought to sell its interest in the sublease it held to the land and the building at 635 Madison Avenue, seeking the sum of \$1,250,000.00 as the price for the assignment of said sublease. In addition, the sublease additionally required annual rental payments of \$393,000.00 on the building and \$60,000.00 on the land.

7. In order to purchase the leasehold from the Milstein Organization, 59th & Madison Realty Corp. was formed. Said corporation executed the sublease agreement.

8. On April 1, 1968, petitioner, 635 Associates, formed a joint venture. The joint venture consisted of 29 members each of whom contributed capital amounting to the total sum of \$850,000.00. The \$850,000.00 was to be loaned to 59th & Madison Realty Corp. so that it would have the capital to purchase the leasehold. The loan from 635 Associates to 59th & Madison Realty Corp. was secured by a leasehold mortgage on said property in the sum of \$850,000.00 and a promissory note in the same amount.

9. The sole purpose of the formation and existence of petitioner, 635 Associates, is stated in Paragraph 3 of petitioner's joint venture agreement which reads as follows:

"3. This Joint Venture is formed for the sole purpose of acquiring the ownership of the aforesaid mortgage and of the aforesaid note and any incidents thereto and to protect and conserve said mortgage and note and to distribute the proceeds received in accordance with the terms of this agreement of Joint Venture and to otherwise take such steps with reference to the investments of the Joint Venture as shall be for the best interest of the Joint Venturers."

10. Accordingly, 59th & Madison Realty Corp. was formed for the purpose of assuming the leasehold obligations in connection with the property involved, and petitioner for the purpose of loaning the corporation \$850,000.00. The stockholders of 59th & Madison Realty Corp. were substantially the same persons who comprised the petitioner, 635 Associates.

11. At the time of filing its New York State Partnership Returns for the years in issue herein, petitioner reported its business to be "Real Estate".

12. Petitioner on its New York State Partnership Returns for the years 1971, 1972, 1973 and 1974 reported the sources of its income to be from :

- Item #6 - Interest (fully taxable for Federal tax purposes)
- Item #11 - Other Income

13. The reported "Other Income" was in amounts as follows:

| | | |
|------|---|-------------|
| 1971 | - | \$32,080.44 |
| 1972 | - | 21,040.00 |
| 1973 | - | 12,000.00 |
| 1974 | - | 4,649.00 |

14. Petitioner reported the source of its "Other Income" for 1971, 1972 and 1973 was from management fees and for 1974 from management and sundry income.

15. Annexed to petitioner's return for 1972 and 1973 is a copy of its 1065 U.S. Partnership Return of Income for 1972 and 1973, respectively.

16. Petitioner on its New York State Partnership Return for the year 1975 reported its only income on Item 6 - Interest (fully taxable for Federal tax purposes). The source of this income was interest on the aforementioned mortgage.

17. The entire amount of the "management fees" was paid to petitioner by a company known as National Cleaners Corporation (hereinafter "National").

18. National occupied space for the storage of their cleaning supplies and equipment, etc., in the sub-basement of 635 Madison Avenue. National serviced 635 Madison Avenue and 654 Madison Avenue.

19. Petitioner asserted its accountant did not know what to do with the rental and/or management fees that National paid, so he credited it to petitioner's account and entered it on their books and tax returns as miscellaneous income for supervisory "management fees". Petitioner contended the accountant made the decision to treat said income in this manner on his own initiative and without petitioner's consent.

20. The accountant for petitioner and for 59th & Madison Realty Corp. was one Milton Seigel, presently retired and living at an unknown location in Florida.

21. Philip Smith, one of petitioner's principals, testified that petitioner did not perform any function for the rental income.

22. Philip Smith further testified that at no time did petitioner supervise or manage the building at 635 Madison Avenue, nor did it ever manage any other property nor was it in the cleaning business nor was it in any other business.

Petitioner failed to offer any real probative evidence of the true basis for the "management fees" (other income).

24. Subsequent to the filing of the returns in issue herein, the State Tax Commission, on August 26, 1977, in a similar fact situation, sustained the tax deficiencies against petitioner for the tax years 1968, 1969 and 1970 (File No. 13881).

CONCLUSIONS OF LAW

A. That Tax Law, section 703(a), defines an unincorporated business as "any trade, business or occupation conducted, engaged in or being liquidated by an individual or unincorporated entity, including a partnership...".

B. That petitioner describes its activities as those of a passive investor. However, in actual fact, petitioner's total "Other Income" (management fees) for the years 1971, 1972, 1973 and 1974 was income from payments to petitioner for purposes petitioner has not wished to divulge. Presumably payments to petitioner totaling \$69,769.44 by National were in some way linked to petitioner's real estate business. That petitioner may not have performed services for National is not conclusive as to petitioner's real tax status. Petitioner was engaged in a business for the years 1971, 1972, 1973 and 1974, whatever its nature, and therefore is subject to the unincorporated business tax. (In the Matter of the Petition of 635 Associates, State Tax Commission, August 26, 1977).

C. That petitioner has the burden of proving it was not conducting an unincorporated business; this it failed to do for the years 1971, 1972, 1973 and 1974. (see section 689(e) of the Tax Law).

D. That petitioner did not have any business transactions that would render it liable for unincorporated business taxes for 1975.

E. That petitioner seeks exemption under section 703(e) of the Tax Law, which provides that an owner of real property, lessee, or fiduciary shall not

be deemed engaged in an unincorporated business solely by reason of holding, leasing or managing real property. Since petitioner is not an owner, lessee or fiduciary, section 703(e) is not applicable.

F. That the petition herein is denied and the Notice of Deficiency dated March 13, 1980, for the years 1971, 1972, 1973 and 1974 is sustained and that the petition herein is granted and the Notice of Deficiency, dated March 16, 1979, for the year 1975, is cancelled.

DATED: Albany, New York

JAN 29 1982

STATE TAX COMMISSION


PRESIDENT


COMMISSIONER


COMMISSIONER